

**Secured Transaction Codes: An Important Tool for  
Tribal Economic and Housing Development**

By Sue Woodrow

Community Affairs Senior Project Director, Helena Branch  
Federal Reserve Bank of Minneapolis

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There is growing discussion in Indian Country about the benefits of commercial codes. Often referred to as *UCCs*, they are important tools for enabling and supporting tribal economic and housing development by improving access to commercial and consumer credit. This article lends support to these discussions by explaining what commercial codes—and, more specifically, secured transaction laws—are and what they do. It discusses how secured transaction codes can help lessen or eliminate some of the significant barriers frequently faced by tribes, Native-owned private businesses and Native consumers when they try to borrow money or make purchases on credit from outside lenders and other businesses. In addition, the article notes several examples of secured transaction codes that tribes around the country have enacted, in some cases highlighting issues they raise. Finally, the article provides information about an important initiative currently underway by the National Conference of Commissioners on Uniform State Laws (NCCUSL) to draft a comprehensive model tribal secured transaction code and companion implementation guide.

Economic development and affordable housing needs are among the most critical of issues faced in much of Indian Country today. Tribal conferences, summits and workshops on these topics are being held nearly every week somewhere in the U.S. While the specific issues, policies and strategies may differ from tribe to tribe and region to region, certain obstacles to affordable housing and economic development, as well as solutions to those obstacles, tend to be common across Indian Country. One significant barrier frequently faced by Native-owned businesses and Native consumers on reservations or in Indian communities is the lack of access to affordable credit for business, housing or other consumer purposes. Credit, of course, is essential for housing purchases and for the development of both tribal enterprises and Native-owned private businesses, particularly in an environment in which reliance on federal and private grant money is lessening, due both to increasing competition for fewer grant dollars

and a growing awareness that the “federal grant” approach to economic and housing development has proven to be only minimally effective.

The importance of credit as a fundamental component of economic and housing development cannot be overstated. Market economies around the world depend on the ability of private businesses, government entities and individual consumers to borrow money or purchase goods and services on credit at affordable rates and on competitive terms. Where laws governing secured lending are insufficient or absent, there will be limited access to affordable credit. Small businesses are hit especially hard by the scarcity of low-cost and long-term credit. That impact negatively affects the whole economy, as the lack of credit and new investment in business limit productivity, in turn impacting both business and personal income growth.

To effectively enable access to credit by businesses and individuals, rules are needed to govern lender-borrower, or creditor-debtor, transactions and relationships. Central to systems for borrowing are rules that protect creditors’ rights, such as those governing when and how debts can be collected. Modern market economies around the world have developed three basic systems for protecting creditors’ rights: unsecured lending, secured lending and mortgage, or land-based, lending. The first system, unsecured lending, is simply an extension of credit to a borrower without requiring collateral.<sup>1</sup> A credit card purchase, for example, is generally an unsecured lending transaction.<sup>2</sup> The second system, mortgage lending, involves the use of *real* property (land or things attached to land) as collateral to secure a creditor’s interest. The purchase of a home typically involves taking out a mortgage, where the home and

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<sup>1</sup> *Extension of credit* includes but is not limited to loans, purchases made on credit, and certain types of leases and consignments. *Collateral* means property in which a debtor has given its creditor a legal interest to secure an extension of credit that will serve as a secondary source of payment in the event the debtor defaults.

<sup>2</sup> Most credit card agreements do not require that the users provide collateral to secure purchases made with credit cards.

often the land on which it is built or attached serve as the collateral for the loan. If a borrower defaults, the holder of the mortgage can foreclose and take possession of the home and/or land.

The third system, secured lending, relies on the use of *personal* property (generally everything other than real property) as collateral to secure a lender's or creditor's unpaid interest. In other words, a debtor's promise to pay is backed by collateral that a creditor can seize and sell in the event a debt is not paid as agreed. This interest in collateral is called a *security interest* or *lien*, depending on whether the interest arises as a matter of agreement between the parties or as a matter of law. Many developed, private market economies, including the United States and the various states individually, have laws that automatically create security interests in personal property in specified circumstances. These are commonly referred to as *statutory liens*. A construction lien or mechanic's lien, for example, arises automatically as a matter of law in many jurisdictions when certain types of services are performed on a credit basis. A tax lien is another example. While important, these laws and the interests they create for the most part fall outside the scheme of secured transaction laws.

Secured transaction law, on the other hand, deals with *consensual* security interests in personal property. Security interests can be either *possessory* (physically held or controlled by the creditor) or *non-possessory*, in which case public notice of the interest in a central filing system is generally required to establish a creditor's priority over competing interests in the same collateral.

Let's look at this concept more closely. First, and as noted above, types of property that can be used as collateral and that are typically covered under a secured transaction scheme include broad categories of

property *except* land or things attached to land (immovable things).<sup>3</sup> Second, the security interests that are created under this system are consensual, meaning they are created by agreement, or by contract, between a creditor and debtor. They do not automatically arise as a matter of law like the statutory liens noted above. Third, security interests under this scheme can be possessory, meaning the creditor takes physical possession or control of the collateral and holds it until the debt is paid; or nonpossessory, where the creditor has a legal interest in the collateral but does not have actual possession or control of it.<sup>4</sup> In the latter case, secured transaction systems generally include a public filing or registry system in which a creditor will publish notice of its nonpossessory security interest.<sup>5</sup> This accomplishes two things. First, it puts other potential creditors of a given debtor on notice that the debtor's property in question is already being used as collateral for another debt or debts. Second, it establishes a "first-in-time" method by which to determine which creditor, if there is more than one, will have a first, or "prior," interest in that collateral.

Secured transaction law in the United States falls generally within the jurisdiction of the various states and not the federal government, and is encompassed in Article 9 of the Uniform Commercial Code (UCC) as adopted by each state.<sup>6</sup> The model UCC was drafted in the 1940s by the NCCUSL for the purpose of

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<sup>3</sup> Generally, a mortgage loan is required to purchase a home or land on credit. However, the purchase of a manufactured home on credit where the home is not permanently affixed to a foundation may be deemed a non-mortgage secured transaction. It may be beneficial for a tribe to enact a secured transaction law that specifies this, particularly if there is a significant amount of trust or other restricted land within the jurisdiction of the tribe that is subject to the BIA mortgage approval process. If a credit transaction to purchase a manufactured home that is not to be affixed to its foundation falls within the tribe's secured transaction law and is therefore not deemed a mortgage transaction, the transaction will probably not be subject to the BIA mortgage approval process.

<sup>4</sup> The significance of a secured transaction scheme that allows nonpossessory security interests is that it expands the types of borrowers and collateral, and thus the types of business transactions, under which creditors will be protected, including installment buyers, borrowers who hold rights to future goods, holders of documents of title and commercial paper (like car titles and loan documents), holders of accounts receivable, buyers of goods yet to be manufactured, and holders of intellectual property rights (such as copyrights and patents).

<sup>5</sup> Most states locate their public UCC filing systems in the offices of their respective secretaries of state.

<sup>6</sup> The UCC provides model articles, enabling individual state legislatures to modify provisions within the code to address their unique concerns, situations and policies. While the various states' UCCs are considered uniform, they

establishing a reasonably consistent legal environment for commercial transactions between the states. Among the reasons for development of a model, uniform commercial code for the states, two were key. First, economic development was being increasingly hampered by nonuniform state laws that were creating obstacles for cross-border commerce between the states. Second, the states were concerned that inaction on the part of their respective legislatures to find solutions to this problem would provide the federal government reason to intervene by passing federal commercial legislation, a solution that states did not want to see happen. Accordingly, the NCCUSL undertook the more than decade-long initiative to create a model uniform commercial code that is made up of twelve separate but complementary articles.<sup>7</sup> As noted above, secured transactions are covered in Article 9.<sup>8</sup>

Secured transaction laws are not an American phenomenon, however. Because the ability of businesses and consumers to access credit and capital is a basic building block of private markets, almost all countries with established market economies have secured transaction systems. Countries around the world that are transitioning from centrally controlled economies to the free market, notably those nations that once made up the former Soviet Union, have made the adoption of secured transaction laws a priority to attract outside investors and business partners. Some of these countries recognize that earlier efforts to promote economic development have been hindered by the lack of secured transaction legislation.<sup>9</sup> Because they do not have adequate laws in place that govern creditors' rights, many countries in Latin America have experienced severe negative impacts on their respective economies in the form of

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do differ to varying degrees. These differences, however, do not appear to have caused material problems for interstate commerce.

<sup>7</sup> Other substantive articles of the UCC cover sales, leases, negotiable instruments, bank collections, funds transfers, letters of credit, bulk sales, documents of title, and investment securities.

<sup>8</sup> Article 9 of the UCC was substantially revised in 1999 based on the efforts of a NCCUSL drafting committee that met 15 times between 1993 and 1998. All 50 states have adopted the revisions to Article 9.

<sup>9</sup> Examples of Central and Eastern European countries that have made secured transaction legislation a priority include many nations that were once Soviet republics or were closely allied with the Soviet Union, including Albania, Ukraine, Georgia, Kazakhstan, the Kyrgyz Republic, Uzbekistan, Romania and Azerbaijan.

prohibitively high costs of commercial credit. They are now in various stages of reforming their respective legal frameworks to address this deficiency.<sup>10</sup> Similarly, many Asian nations, still reeling from the Asian economic crisis of the last decade, have begun legal reform measures to address the lack of creditor protections.<sup>11</sup> So critical is the need for transitioning and developing countries to adopt secured transaction legislation that the United Nations General Assembly, in a 2003 report, stated that the United Nations Commission on International Trade Law should assist countries “in adopting modern secured transaction legislation, which was generally thought to be a necessary . . . condition for increasing access to low-cost credit, thus facilitating the cross-border movement of goods and services, economic development and ultimately friendly relations among nations.”<sup>12</sup>

So why are secured transaction laws important for economic development in Indian Country? The pervasive lack of access to affordable credit and capital in Indian Country can be generally attributed to the fears and apprehensions routinely expressed by non-Native lenders and other potential business partners and investors. Those fears typically include concerns, perceived or otherwise, that tribal law is either lacking or is insufficient to adequately protect their interests in collateral located in a tribe’s jurisdiction; that tribal courts will not provide a fair or informed forum to resolve disputes that lenders may have with borrowers within a tribe’s jurisdiction; or that lenders will not have effective recourse, in the event of default, to take possession of collateral held within a tribe’s jurisdiction, even if there are laws in place that purportedly provide protections to lenders. Faced with uncertain or no rules, lenders are hesitant or unlikely to lend to borrowers on reservations or in Indian communities, or may do so but on more restrictive terms and at interest rates that far exceed those for loans to off-reservation borrowers.

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<sup>10</sup> Latin American countries now in various stages of working on creditors’ rights law reform and related insolvency and bankruptcy systems include Mexico, Argentina, Bolivia, Ecuador, Colombia, Honduras and Peru.

<sup>11</sup> China, Thailand, Vietnam and Indonesia are among several Asian countries embarking on creditors’ rights legal reform.

Indeed, this has been a persistent problem throughout Indian Country. Sometimes these loans may simply be discriminatory. Often, however, the terms and rates merely reflect the increased risks involved in providing credit in situations in which there are inadequate legal and procedural protections. As elsewhere in the world, the availability of low-cost credit is suppressed where lenders encounter inadequate or no laws that effectively guarantee their loans against collateral.

As in the developing and in-transition nations highlighted earlier, fundamental to the goal of building sound economies is the need for commercial laws that will enhance tribal business environments by reducing risks for outside lenders and other nontribal entities that do business with tribes, tribal enterprises, Native-owned private businesses and Native consumers. Tribal commercial laws will more effectively help achieve these goals if they are sufficiently similar, or harmonized, with the laws of neighboring states and tribes, as cross-border business can be transacted more efficiently and cost-effectively when the law of the tribal jurisdiction in which outside parties are doing business is familiar to those parties.

A number of tribes have adopted secured transaction codes, or UCCs. Some have modeled their codes on Article 9 of the model UCC, while others have used Article 9 as adopted by the state in which the tribe's reservation or community is located as their template. Some tribes have adopted verbatim the law of the state in which they are located as tribal law. These tribes have incorporated the state law by reference into tribal law, in some cases carving out a few provisions or making the state law subject to a few specified tribal laws. A number of tribes have modeled their codes after the model tribal code drafted by the

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<sup>12</sup> Official Records of the General Assembly, United Nations Commission on International Trade Law, A/CN.9/543, September 2003.



University of Montana's Indian Law Clinic.<sup>13</sup> Others have adopted either the uniform Article 9 or the state Article 9 for a specific transaction only. And finally, a few tribes have adopted more narrowly purposed collection codes that govern repossession procedures only.

While each of these approaches most certainly offers benefits in theory or in practice, each has drawbacks. In the cases where tribes have either modeled their secured transaction laws after the model UCC Article 9 or a particular state's Article 9, or have incorporated either the model code or state law by reference as tribal law, it is likely that even where specific carve-outs of certain provisions have been made, the tribes have unknowingly adopted components of state law or common law that, if truly understood, would not be desired or may actually conflict with other tribal law, custom or tradition.<sup>14</sup> To those inexperienced in commercial law, these references and what they mean may not be apparent, at least until a legal issue arises. In such an event, a tribal court may be faced with the difficult choice of either upholding the law as adopted, with an unintended and undesirable outcome, or making the "right" decision pursuant to conflicting tribal law, custom or tradition, notwithstanding the letter of the law as adopted; and, thereby, risking the court's credibility with outside parties.

The Montana Model Tribal Secured Transaction Code was drafted in such a manner as to avoid these types of inadvertent "incorporation of other law by reference" issues. Extensive work was done to address tribal business and cultural needs and expectations. That model code, however, was drafted prior to the

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<sup>13</sup> [www.umt.edu/lawinsider/library/lawbysub/ucc.htm](http://www.umt.edu/lawinsider/library/lawbysub/ucc.htm)

<sup>14</sup> Model Article 9 and Article 9 as adopted by the various states incorporate by reference a significant amount of "law" from outside the Article itself. For example, Article 9 does not determine whether a person has transferable rights in property, but leaves that determination to other law. If a person does not have transferable rights in property, that property cannot be used as Article 9 collateral. However, for some purposes, Article 9 overrides other law that restricts assignments, notably that which relates to payment rights. So, for example, if a tribe has a law that prohibits a person from assigning his or her per capita distributions to another party, as a consumer protection measure, adoption of Article 9 with this provision rendering such a restriction ineffective would, in effect, render the

finalization of the significant revisions that were made to Article 9 by the NCCUSL several years ago and that have subsequently been adopted by all of the states. Therefore, tribes that have modeled their secured transaction laws on the Montana model will probably find that their laws are no longer consistent with state law in many significant respects. This may or may not prove to be an issue with outside lenders. Finally, those tribes that only have collection codes in place and are therefore only addressing the process by which outside creditors may take possession of collateral located within the tribe's jurisdiction are missing many of the critical components that compose a comprehensive secured transaction law.

In response to requests from a number of tribes for assistance in developing an up-to-date model tribal secured transaction law, and in recognition of the problems inherent in the wholesale adoption by tribes of the model UCC or state law versions, the NCCUSL embarked on an effort to draft a comprehensive secured transaction code specifically tailored for tribes, with the intent of addressing the issues highlighted above. The drafting committee and participating advisors make up a group that includes experts in secured transaction law, tribal attorneys and other tribal representatives who understand their respective business and financing environments, and other legal experts who work in Indian Country.<sup>15</sup> Together, the committee has the extensive and varied expertise necessary to draft a law that accomplishes a fourfold objective: 1) to harmonize state law and tribal law to address concerns about unfamiliar or insufficient law as commonly voiced by outside lenders and investors; 2) to eliminate the potentially harmful "incorporation of other law by reference" problems noted above; 3) to address specific needs and

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tribal law restriction void. In addition, Article 9 incorporates by reference a substantial amount of "law" from the other UCC Articles.

<sup>15</sup> Advisors to the drafting committee have included tribal attorneys, tribal business representatives and outside counsel from the Sac and Fox Nation, Cherokee Nation, Navajo Nation, Affiliated Tribes of Warm Springs, Chitimacha Nation, Oneida Nation and several California Rancherias and Alaska Native communities.

concerns that are unique to tribes; and 4) as with the states, to enable tribes to avoid the considerable time and expense involved in drafting commercial laws.<sup>16</sup>

The committee intends to have the draft completed by early 2005. In addition, a comprehensive implementation guide is being drafted to accompany the model code. The guide will provide a plain-language commentary on each code provision, list optional provisions where the committee is aware that tribes may have differing needs or issues, offer guidance to tribal legislative bodies for adopting the code as tribal law, and serve as a general educational tool for tribal judges and attorneys as well as tribal credit, economic development and business managers.

It is important to note that while adoption of a comprehensive and culturally tailored secured transaction law is an important step in creating a strong and sustainable tribal business environment, it alone is not sufficient to accomplish this objective. Equally important are tribal courts that are perceived to be fair and impartial and that are competent to adjudicate commercial cases. Independent courts that are not subject to the wiles of elected officials are generally perceived much more favorably by outsiders. Also, lenders and other potential business partners want assurance that tribal judges understand the complexities of the commercial laws they may need to adjudicate. Because many tribal judges and attorneys have traditionally adjudicated and advocated primarily in areas of criminal and family law, education and training are absolutely critical if a tribe adopts a secured transaction law.

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<sup>16</sup> A sample of some of the unique issues addressed in the model tribal code include choice of law and choice of venue, filing systems, no or limited waivers of sovereign immunity, self-help remedies, implication of tribal liens, role of tribal custom and tradition, optional limitations on per capita distributions as collateral, treatment of fixtures and manufactured homes, and consumer protections such as limitations on the ability of persons to enter into agreements with tribal consumers that do not comply with a tribe's secured transaction law.

Also critical is the need for tribes to provide easy access to their laws and court decisions, either by publishing them on a Web site or in readily accessible written format. Business is likely to be hindered if an outside party cannot access a tribe's law or does not know it exists. Similarly, tribal court decisions should be published and accessible so parties can determine how a tribal court is interpreting the law. Every obstacle an outside party encounters in this regard when considering a business transaction within a tribe's jurisdiction will increase the likelihood of having unfavorable business terms or no deal at all.

In sum, a comprehensive and culturally appropriate secured transaction code can be an important tool for tribes, Native-owned businesses and Native consumers that are encountering barriers to affordable credit. The NCCUSL initiative can assist tribes that are considering adopting a secured transaction code. The NCCUSL's objective is to produce a model tribal code that will be responsive to tribes' expressed desire for a comprehensive model law that is specifically tailored to the multitude of tribal needs and issues, yet is sufficiently harmonized with state law so as to eliminate some of the significant barriers that tribes and their members currently face with outside lenders. It is the intent of the NCCUSL that through the adoption and implementation of the secured transaction code, tribal enterprises, Native-owned private businesses and Native consumers in Indian Country will gain opportunities to access the affordable financing they need to realize their housing, business and other economic development objectives. It is also the hope of NCCUSL that the model code will prove to be a culturally and legally appropriate tool that, when adopted and implemented, will support and strengthen the effective exercise of tribal sovereignty.